siders' notorious proposal for a phony gold standard. In that scheme, the public would not be able to redeem its dollars in gold coin, the Fed would continue to manipulate and inflate, but all the while this inflationist policy would now be cloaked in the confidence-building mantle of gold.

In both plans, we would be dazzled by the shadow, the rhetoric of sound policy, while the same old program of cheap money and huge deficits would proceed unchecked. In both cases, the dominant ideology seems to be that of P. T. Barnum: "There's a sucker born every minute."

How Government Intervention Plagued Our 19th-Century Economy

Lawrence W. Reed

The recessions and depressions of the 19th century are often cited as proof of the "inherent instability" of the free market. (Indeed, the promoters of the Federal Reserve System in 1913 argued for a central bank as a way of preventing future downturns!) This is, of course, a bum rap.

The 1800s were freer than today, but there was more than enough government intervention to cause serious setbacks in the economy. And Austrian trade cycle theory explains exactly how.

The source of the business cycle, Mises discovered, is government-engineered expansion of money and credit. Such a policy artificially depresses interest rates at first, deranges the structure of production by generating unsustainable malinvestments, and inevitably leads to contraction and painful readjustments.

The first economic calamity of the century occurred in 1808 when a federal embargo on overseas shipping produced

widespread bankruptcies and unemployment. After that, five major cyclical depressions struck the American economy: in 1819, 1837, 1857, and 1893. The typical economic history text lists among the "causes" things like railroad speculation, stock crashes, trade imbalances, commodity price booms and busts, etc.

These are not, of course, causes at all, but merely symptoms. Only Austrian trade cycle theory as propounded by Ludwig von Mises, Murray N. Rothbard, and others, makes sense of the mess and provides a coherent explanation of these five depressions.

The 1819 collapse followed a flagrant credit expansion by the Second Bank of the United States, created by the feds in 1816. The definitive work on the experience is still Rothbard's PhD thesis, *The Panic of 1819.*

Rothbard documented the extensive culpability of the Second Bank. In its very first year, it issued $23 million on a specie reserve of about $2.5 million. The expansion of credit, which eventually involved state banks as well, was actively encouraged by the U.S. Treasury. The government even made it legal for inflating banks to fraudulently suspend payment of specie, ripping off hapless depositors in the process.

Then, in a series of deliberate deflationary moves, the Second Bank pulled the rug out from under the very house of cards it had built. It forced a drastic reduction in the money supply starting as early as the middle of 1818. The depression, which came a few months later, was the unavoidable outcome of gross manipulation of money and credit.

Those who blame the gold standard for this debacle are wrong. In fact, the country was not even on a gold standard at the time. In 1792, the official policy was "bimetallism," according to which silver and gold were to circulate side by side at a governmentally fixed ratio. (The ratio between the prices of any two commodities, including gold and silver, is always changing on the market, and an attempt to fix the ratio by

government fiat always leads to trouble. In this instance, it forced the country onto a de facto silver standard from the start. The same sort of intervention proved to be a major factor in the later crisis of 1893.)

The Second Bank's shenanigans created the depression of 1837. Anticipating a political battle to renew the Bank when its charter ran out in 1836, Bank authorities early in the decade embarked upon a rapid expansion of the money supply. Reserve ratios were pushed to their lowest levels of the entire antebellum period. Orchestrating "good times" through easy money was the Bank's way of fighting hard-money, anti-central bank President Andrew Jackson.

Jackson, however, flattened the inflation by requiring specie in payment for federal lands and by vetoing the Bank's charter. In the quick contraction that followed, the inflationary malinvestments promoted by the bank were liquidated. But Washington persisted with its policy of bimetallism. In addition, state and local governments responded to the 1837 collapse with a wave of anti-banking laws, outlawing banks altogether in some places and exacerbating the depression. This is hardly laissez-faire or gold standard behavior.

By the early 1850s, state governments got into the inflation act. Exerting control over their extensive network of state-chartered banks, they pressured the banks to monetize state debt. The result was another round of credit expansion, dangerous reduction of specie reserves, and a temporary, artificial boom in the economy, followed by panic and depression in 1857. Because the pressure on banks to monetize debt occurred principally in the Northern states, the subsequent collapse was considerably less pronounced in the South.

The general depression of 1873 also provides a clear example of government as the guilty party. In the prior decade, both Northern and Southern regimes abandoned a specie standard altogether and printed massive quantities of irredeemable, legal tender paper.

In the Confederacy, high taxes, a paper hyperinflation, and Northern scorched-earth military policies plunged the region into depression in 1865.

In the North, despite crippling tax hikes, revenues fell far short of the funds necessary to prosecute the war. No less than $5.2 billion in "greenbacks" were printed. At the war's conclusion, a greenback dollar was worth only 35 cents in gold. The Northern economy struggled for a few more years, but with the complete cessation of paper inflation in the 1870s, collapse and readjustment began by 1873.

Recovery had barely commenced when the central government began a new form of monetary intervention, this one tied to silver. In 1878, Congress passed (over President Hayes's veto) the Bland-Allison Act, which mandated the Treasury's purchase of $2-$4 million in silver bullion per month. The metal was to be minted into silver dollars, each containing 371.25 grains of silver. Since the gold dollar was defined as 23.22 grains of gold, this established a ratio between the two metals of 16 to 1.

But the free-market value of silver in terms of gold was at least 18 to 1 in 1878. By overvaluing silver and undervaluing gold, Bland-Allison set Gresham's Law into motion. "Bad" money (officially overvalued silver) began to drive "good" money (officially undervalued gold) out of circulation, deranging the nation's finances and engendering a steady loss of confidence in the currency. On top of it all, Bland-Allison authorized the Treasury to issue paper silver certificates along with the depreciating silver dollars.

The inflationists of the period—who pushed for this intervention in the belief that "more money" would aid the economy in general and debtors in particular—were not satisfied. Throughout the 1880s, they pushed for even more inflation under the guise of "doing something for silver."

Their crowning folly was enacted into law in 1890—the Sherman Silver Purchase Act. It required the Treasury to

buy virtually the entire output of American silver mines—4.5 million ounces per month; mint it at 16 to 1 at a time when the gold/silver ratio in the free market was actually greater than 30 to 1; and issue new paper "Treasury Notes" simultaneously.

Drugged by easy money, the economy took on the classic symptoms of a boom. Unemployment and interest rates in 1891 and 1892 fell dramatically. Capital goods industries worked feverishly. Foreigners, however, were the first to sense danger and began withdrawing their capital from America as early as 1891.

The economic reversal started in 1893, and led to the worst depression in 50 years. It also produced one of the more scholarly addresses ever delivered before the House of Representatives. Congressman Bourke Cochran of New York, a first-rate historian, traced the history of coinage in England and explained how debasing the currency led to recurrent depressions. Applying that principle to his day, he declared:

> I think it safe to assert that every commercial crisis can be traced to an unnecessary inflation of the currency, or to an improvident expansion of credit. The operation of the Sherman Law has been to flood this country with paper money without providing any method whatever for its redemption. The circulating medium has become so redundant that the channels of commerce have overflowed and gold has been expelled.

Viewing the crisis of 1893, contemporary historian Ernest Ludlow Bogart said:

> It must be said that the net results of this experiment of "managed currency," that is, one in which the government undertakes to provide the necessary money for the people, were disastrous. For the maintenance of a suitable supply, the operation of normal economic forces is more reliable than the judgment of a legislative body.

The economy of 19th-century America was punctuated by serious economic setbacks. They were caused not by the free market, but by the destructive manipulations and interventions of government authorities. This was not a century of government as innocent bystander, but of government as the incessant bungler, running roughshod over the principle of sound and honest money. (Although, without a Fed and other government interventions, the recoveries from these panics were quick.)

We can learn much from the experiences sketched here. Monetary reform, if it is to be genuine and successful, must sever money and banking from politics. That's why a modern gold standard must have: no central bank; no fixed rations between gold and silver; no bail-outs; no suspension of gold payments or other bank frauds; no monetization of debt; and no inflation of the money supply, all of which have proved so disastrous in the past.

Anything short of the discipline and honesty of a true gold coin standard will inevitably self-destruct, consuming our wealth and liberties, and nurturing the omnipotent state.

Send Out the Clowns

Llewellyn H. Rockwell, Jr.

Only in the cloud cuckoo-land that is Washington, D.C., could the budget summit held by the Congress and the Reagan administration be taken seriously.

After the Crash, the politicians panicked. Not because of any harm to the American people, but because such events can hurt all incumbents. The result was a sideshow that—not unsurprisingly—has *not* calmed the markets.